In the Supreme Court
OF THE
United States

October Term, 1940

No.

Pacific National Bank of San Francisco, a national banking association, et al.,
Petitioners,

vs.

Merced Irrigation District,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I. FACTUAL BACKGROUND OF THE CASE.

A brief history of Merced Irrigation District up to 1929 appears in Exhibit OO, pages 118-139.[1]

[1]Exhibit "OO" is the transcript of record presented to this Court in the previous action between these parties (under the first Municipal Bankruptcy Act), entitled "Merced Irrigation District, The Reconstruction Finance Corporation, et al., Petitioners, v. Reed J. Bekins and Milo W. Bekins, et al., Respondents", No. 206. This record, consisting of one volume, is (by stipulation and with the approval of the Clerk of this Court) treated as a part of the record in the present proceeding.

The respondent, Merced Irrigation District, was organized late in 1919 (Ex. OO, p. 118).

Considered geographically, the District contains over 189,000 acres, being "The fifth largest district in California, and one of the most important" (Ex. OO, p. 119).

The original estimate in 1921 of the cost of buying and constructing the works of the District was $15,850,000 (Ex. OO, p. 121). Ultimately it was found necessary to issue bonds for a total of $16,250,000 (Ex. OO, pp. 121, 123).

The District purchased the properties of a private water company operating in the District (irrigating a maximum of 40,000 acres), and constructed the Exchequer dam in Merced River, a hydro-electric plant, and an extended irrigation system. The Exchequer dam is one of the largest in the country, and when completed in 1926, was said to be the highest dam in the world (Ex. OO, p. 128; R. 682).

The power plant was completed late in 1926 and has been in full operation ever since. The District sells its power to a private water company under a contract to expire in 1964, and has received for its power an average of $445,000 per year up through the year 1938. The revenue derived from power depends on the amount of power produced, and the amount produced depends in turn on rainfall. The period of operation so far, includes the lowest average rainfall of any consecutive nine-year period from 1870 to date (R. 535).

The District met all payments of principal and interest on its bonds up to and including payments due January 1, 1933. It has paid nothing since, except some interest to bondholders who surrendered their bonds, and interest paid to the R. F. C. on its loan.

In March, 1932, a Bondholders' Committee was formed, to deal with anticipated default of the District, due to extremely low agricultural prices and low returns during the previous three years from the sale of power because of an unprecedented drought (R. 940).

The chairman of the Bondholders' Committee, from its creation in 1932 down to January, 1935, was a Mr. Keplinger who, though apparently not an officer of the Bank of America, represented its interests on the Committee (R. 506). At the time when the plan here involved (then a voluntary plan) was approved late in 1935, the chairman of the Committee was F. S. Stevenot, an officer and representative of the Bank of America (R. 504).

The Bank of America was not only a bondholder (R. 885, 504), but also owned something over 3,000 acres of land in the District through its subsidiary, Cal. Lands, Inc. (R. 472-3); and was also heavily involved in the District by virtue of holding many mortgages on lands in the District, securing, in the aggregate, a large amount of loans (R. 421, 503; Ex. OO, p. 75).

Immediately upon its creation, the Committee solicited the deposit of bonds under a deposit agree-

ment (R. 576), and a major portion of the bonds was deposited. Mr. Keplinger, as chairman of the Committee, went to Professor Murray R. Benedict, an agricultural economist in the Giannini Foundation at the University of California, and asked him to prepare a report on the condition of the District (Ex. OO, p. 75). Mr. Benedict and others working under his supervision prepared what is herein referred to as the "Benedict Report", which is Volume 4 of the record herein, and is the principal basis of the District Court's contention concerning the fairness of the plan.

On the basis of this report the Bondholders' Committee submitted a plan to the bondholders providing for payment of the entire amount of bond principal, with extensions of maturities and some reduction in interest (R. 576, Ex. OO, p. 91). This plan was approved by the electors in the District (Ex. OO, p. 91); but after the enactment of Section 36 of the Emergency Farm Mortgage Act, providing for R. F. C. loans, the District applied to the R. F. C. (December 16, 1933, R. 600) for such a loan. In November, 1934, the R. F. C. granted a loan of $8,600,000, calculated to pay the bondholders 51.501¢ on the dollar on principal, and nothing for interest in default. The terms of this loan are identical with the terms of the plan here involved.

Whether or not the R. F. C. made an appraisal of the District, and if it did what that appraisal showed, does not appear in the record. Presumably, the R. F. C. followed the statute (43 U. S. C., Sec. 403), which

requires R. F. C. to cause "an appraisal to be made of the property securing and/or underlying the outstanding bonds of the applicant," and which provides that before making such a loan the R. F. C. must be satisfied that the borrower will be able to acquire "a major portion" of its bonds at "the average market price of such bonds over the six months period ending March 1, 1933". Merced bonds had been selling at extremely low figures during this time.

A proposal embodying the terms of the R. F. C. loan was then formulated, and the Bondholders' Committee (which at this time represented over 80% of the bondholders) then sent them a questionnaire, on January 7, 1935 (R. 958) asking whether they desired the so-called "Cash Offer plan, i. e., the plan now before the Court, offering 51.501¢ on the dollar of principal, and nothing for defaulted interest, or the former plan calling for extensions of time, reduction of interest and ultimate payment of the full amount of principal.

In submitting these alternatives to the bondholders, the Committee stated that it thought the cash offer "unduly low", and that whether they should accept it depended upon "the circumstances of the individual bondholders" (R. 496, 498). The majority replied expressing preference for the cash offer plan, which the Committee thereupon voted to accept by a vote of 8 to 5 (R. 501).

Several large bondholders, in addition to the Bank of America, were represented on the Bondholders' Committee, including several of your petitioners

herein. All of these large bondholders, except the Bank of America, withdrew their bonds after the Committee's approval of the cash offer plan (R. 885, 504). Over $14,000,000 in principal amount of bonds were surrendered pursuant to this plan, the former holders accepting 51.501¢ on the dollar in full and final satisfaction of their claims (R. 344).

At that time there were 1200 bondholders, holding an average of $13,500 of bonds each (R. 503).

The first Municipal Bankruptcy Act was passed in 1934, and on April 19, 1935, the District filed a petition under that statute setting forth the cash offer plan (Ex. OO, p. 41). The Bondholders' Committee consented to the plan pursuant to authority in the deposit agreement (R. 584, 593).

The District Court confirmed the plan by its decree of March 4, 1936. An appeal was then taken to the Circuit Court of Appeals. Pending the appeal this Court decided the case of *Ashton v. Cameron County Water Improvement District No. 1,* 298 U. S. 513, holding that the first Municipal Bankruptcy Act was void. Thereupon, on March 16, 1937, these petitioners moved the Circuit Court of Appeals to dispense with the printing of the record and for a judgment of reversal, on the authority of the *Ashton* case (Ex. OO, p. 333). Pursuant to the motion, the Circuit Court of Appeals reversed the decree of the District Court on April 12, 1937, with directions to dismiss (R. 106, 90 Fed. (2d) 1002); and in due course this Court, on October 11, 1937, denied the District's petition for a writ of certiorari (302 U. S. 709). Thereafter, on July 6,

1937, pursuant to mandate (R. 962) the District Court entered its decree of dismissal (R. 965).

In the meantime, the present Municipal Bankruptcy Act had been passed, on August 16, 1937, as Chapter X of the Bankruptcy Act (50 Stat. 654, 11 U. S. C., Secs. 401-404). It is now Chapter IX of the Bankruptcy Act as amended by the 75th Congress, 3rd Session (52 Stat. 840, 939-40).

This new act was upheld in *United States v. Bekins*, 304 U. S. 27, decided April 25, 1938. On June 17, 1938, the present proceeding was commenced under the new statute, seeking confirmation of the identical plan confirmation of which had been sought in the previous proceeding (R. 8, 36; Ex. OO, p. 10).

II. THE PLAN IS UNFAIR BY ANY STANDARD.

In this and in the next Section, we discuss, (a) the amount of the District's debts, (b) the value of its corporate assets, (c) the value of the privately owned lands in the District charged with payment of the bonds, and (d) the District's past, and probable future, income.

The evidence concerning these matters is not exhaustive; and in that connection we call attention to the following propositions:

(a) The trial court has made no finding whatever concerning any of these matters, nor did the court below;

(b) The burden of proof was upon the District to show the plan was fair and equitable, and

in that behalf to show what the facts were concerning the matters above enumerated;

(c) Particularly in the light of the foregoing, we submit that under the rule of *First National Bank v. Flershem,* 290 U. S. 504, 525, and similar cases, the evidence now to be discussed should be considered by this Court unless it intends to grant a new trial.

(a) The District's debts.

The District's total debts on November 1, 1938 (they are not shown as of June 17, 1938, the date action was commenced), amounted to a total of $21,252,-256.47. This includes all debts, whether affected by the plan or not (Ex. Z, R. 886-7). This amount is $1,509,366.26 less than the amount of the District's debts shown on its balance sheet of the same day, that is, of November 1, 1938 (Ex. 26, R. 669). The difference is accounted for by inaccuracies in the District's balance sheet which are corrected by Exhibit Z, as follows (see testimony of the District's Auditor, R. 425-6, 520):

(1) The District's balance sheet states, as owing, the entire amount of the District's unpaid bonds (both matured and unmatured), and as a separate and additional item of debt, states the amount of matured unpaid bonds, amounting to $387,000.00;

(2) In the item of unpaid matured bond interest coupons, the balance sheet includes interest which had actually been paid to depositing bondholders and to the R. F. C. It also includes interest on these two items

of interest which had already been paid. These inaccuracies are shown by, and corrected in, Exhibit Z.

(b) The District's corporate assets.

The District's assets as of the date of the commencement of the action do not appear. They are shown as of a few months later, in the District's financial statement as of November 1, 1938 (Ex. 26, R. 669), which shows the following:

Cash	$ 1,578,446.14
Other current assets	250,661.92
Net capital assets (physical properties)	18,649,793.20
Total	$20,478,901.26
The total should be shown as	$21,318,901.26

The difference between the two amounts consists of an additional item which the District's Secretary admitted must be added to the capital assets shown in the balance sheet (R. 515). This item consists of the aggregate of water rights purchased from customers of the water company which formerly operated in the area, which rights were purchased for a total price of $1,020,000. Of this sum, $840,000 has been paid (R. 510-12, 515). Adding this item to the other assets gives total net assets of $21,318,901.26.

The physical properties included in the balance sheet are valued therein at cost less depreciation (R. 424). There is no evidence in the record of the value of the physical properties other than this evidence, namely, cost less depreciation. In these circumstances, and in

view of the District's burden of proving insolvency, we submit that the minimum value to be given to the District's physical properties (primarily its dam, power plant and irrigation system) is the amount thus shown by the District's books, namely, cost less depreciation. The minimum total of the District's physical properties and other assets is therefore $21,318,901.26.

III. THE DISTRICT'S INCOME IS SUFFICIENT TO PAY A DEBT APPROXIMATELY TWICE THE AMOUNT OFFERED BY THE PLAN.

We now summarize very briefly the evidence of the District's income from each major source. We shall then compute what its aggregate income shows on the subject of ability to pay.

(a) The District's past income from assessments.

The District was organized in December, 1919. Its income from assessments is shown from the beginning. Its income from the sale of power is shown from the beginning of such sales in 1926. Its income from other sources is shown since 1931, but is not shown for the years preceding 1931. The evidence of income stops shortly after the end of the fiscal year 1937-38. From 1920 to 1933, both inclusive, the District levied assessments designed (with its other revenue) to meet its obligations. For the following five years shown in the record the assessments levied were much less in amount, and still are, for two reasons:

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Correction to Brief in Support of Petition for Writ of Certiorari.

Page 35, lines 19 to 23 should read as follows:

"gations. As a result, the District's cash on hand rose from $183,180.46 on December 31, 1933 to $1,578,446.14 on November 1, 1938 (R. 669, 845), the latest date shown; and this notwithstanding the extremely low levies during this period."

(1) Beginning with the levy of 1933-34 and down to the present time the District has operated under Section 11 of the Districts' Securities Commission Act (Cal. Stats. 1931, p. 2263, as amended by Cal. Stats. 1933, p. 355 and as since amended). This is a moratorium statute, relieving districts which have got into difficulties from the necessity of levying assessments sufficient to meet their obligations, and authorizing them, with the approval of the California Districts Securities Commission, to "levy only for such total amount as in their judgment . . . approved by the Commission it will be reasonably possible for the lands in said district, taken as a whole, to pay without exceeding a delinquency of fifteen per cent".

(2) The consummation of the R. F. C. loan, and the surrender pursuant thereto (in 1935) of more than 80 per cent of the District's bonds, materially reduced the amounts necessary to meet current obligations. As a result, the District's cash on hand rose from $188,180.46 on December 31, 1933 to $1,829,106.06 on November 1, 1938 (R. 669, 701), the latest date shown; and this notwithstanding the extremely low levies during this period.

The annual levy prior to the year 1928-29 does not appear for each year, though the total appears. The average annual levy from 1928-29 through 1932-33 exceeded $1,100,000. The average annual levy from 1933-34 through 1937-38 averaged only about $270,000.

More important than the amount levied, in determining ability to pay, is the amount actually paid by the landowners to the District. During the first twelve

years, i. e., up through the year 1932, the landowners actually paid to the District a total of $10,402,666.69 in assessments, or an average of $866,888.39 per annum. This amount, taken with the District's other income, is sufficient, after paying operating expenses, to amortize in thirty-five years, at 4% (the term of the refunding bonds proposed by the plan) more than twice the amount offered by the plan.

If we take the entire eighteen years of the District's life shown in the record, including the early formative years, some very good years that followed, and the very bad years of the depression, the landowners have actually paid, in assessments, an average of $700,421 a year (R. 705, 667).

If we take the last seven years given in the record (1931-37), starting with, and including the whole of, the great depression, we find that the landowners actually paid, in assessments during those seven years, an average of $517,850 per year (R. 829, 837, 846, 853, 863, 873, 881).

And these seven years were far below normal in farm income. Farm prices during this seven-year period (although they have increased steadily every year since 1931, R. 734), were so unprecedentedly low in 1931, 1932 and 1933 as to make the average for the seven years only 86% of the period 1909-14, taken by the federal authorities as normal (R. 733-4).

Moreover, the District has not even pretended to levy anything for bond service during 5½ of those seven years, the rate being from $3 per $100 down to $1 per $100 of assessed value (R. 667).

In the year 1932, when agricultural prices fell to their lowest point (44% of the 1909-14 average, R. 734), and when the District levied the highest rate in its history, resulting in a 62% delinquency, the landowners actually paid, in assessments, $578,110.38 (R. 837).

(b) The District's power revenue.

It cannot reasonably be contended that the District's revenue from power will average less than $500,000 per year.

1. Two careful and exhaustive studies by recognized authorities were made (R. 890-948, 524-38). One is based on the run-off of the Merced River from 1902 to 1938, both inclusive, and shows an average revenue under the District's present power sale contract (which runs until 1964), of $511,651 per year (R. 937). The other study, which carried the computation back to 1871 shows average revenue of $534,000 per year (R. 534).

2. The District itself reported to the R. F. C. that it is reasonable to assume that its future power revenue will average between $500,000 and $621,000 per year (Ex. OO, pp. 103-105).

3. Figures supplied by the District to the Districts Securities Commission, estimated in 1936 that the power revenue for 1937 would be $500,000 (R. 728); and estimated in 1937 that the power revenue for 1938 would be $500.000 (R. 783). The amount actually received in each of these years was more than $500,000 (R. 937).

The only evidence the other way consists of the fact that during the period of actual operation, 1926-38, which includes the lowest consecutive nine years of run-off since 1871 (1926-34, R. 937, 535), the average power revenue was only $445,000 (R. 933, 937).

It is plain, we submit, that in determining probable ability to pay, the District's power revenue cannot fairly be taken as less than an average of $500,000 per year.

(c) The District's revenue from miscellaneous sources.

During recent years the District's revenue from miscellaneous sources (land rentals, water tolls, interest, and miscellaneous revenue) has averaged about $80,000 a year (R. 863, 873, 881).

(d) The District's operating expenses.

The only testimony concerning operating expenses is that of the secretary of the District, who testified, in the former bankruptcy proceeding, that annual operating expenses would amount to a total of $400,000, excluding payments on certain drainage bonds now fully paid, and payments on Crocker-Huffman contracts which will be fully paid next year (Ex. OO, p. 63; R. 694-5). In this proceeding he raised this to $500,000, explaining the difference by additional proposed capital improvements of $30,000 per year, and some increase in labor costs (R. 515). This figure includes drainage bond payments and Crocker-Huffman payments, amounting to about $50,000 per year

(R. 874, 883), both of which will have ceased entirely next year (R. 694-5).

The testimony is not directly contradicted, for the bondholders have no means of doing so; but it is contradicted by the undeniable fact that the District's actual operating expenses averaged only $401,134.43 (R. 864-5, 873-5, 881-3), for the last three years shown in the record notwithstanding the fact that during these years the District had a very large surplus of cash on hand (Ex. X, R. 827, 862, 876, 880), and had no reason, therefore, to defer proper expenditures.

Moreover, the secretary's estimate of operating expenses includes $125,000 per year for capital improvements, which we submit cannot be considered in determining the ability of the District to pay its debts.

The District's own estimated operating expenses (including capital improvements), for 1938, reported to the R. F. C., were less than $425,000 after eliminating payments on drainage district bonds which the District took over and which are now all paid, payments on Crocker-Huffman contracts which will all be paid off next year, and refinancing expenses (R. 774, 783, 694-5).

(e) The District's net income as indicating ability to pay.

The plan proposes a 4% bond issue with maturities running from 1941 to 1975 (R. 202, 204). Taking this plan as a standard, it is a simple matter of computation from the foregoing figures concerning the District's past and probable future income, to show that even taking the most pessimistic view, it would

be impossible reasonably to conclude, on the basis of past experience, that the District cannot pay a great deal more than its plan offers.

The last seven years, shown in the record (1932-1937), is the worst available sample upon which to base an estimate of future income, primarily for two reasons:

(1) During five of those seven years, the total assessments levied were much less than half of what the bondholders have actually paid on the average during the District's entire existence (R. 667).

(2) This seven year period includes the worst of an unprecedented depression in agricultural prices, now past (R. 733).

Notwithstanding this, the fact is that the average annual amount of assessments actually paid to the District during that seven year period was $517,850, as shown above. And if we assume that future power revenue will be only $450,000 (which is plainly too low), and assume that future operating expenses will be $450,000 (which is plainly too high), the income of the District will be sufficient to discharge a debt of $11,209,687 at 4% in thirty-five years, namely, $2,869,687 more than the plan proposes to pay, i. e., $8,338,011.

In the light of all the foregoing, it is plain that any reasonable estimate of future income, based on past experience, calls for the conclusion that the District's income will be sufficient to discharge (at 4%, in thirty-five years), a debt at least twice the amount which the plan proposes to pay on those terms.

(f) The District's evidence concerning ability to pay.

The District, as well as both courts below, relied for showing that the plan is fair upon the so-called "Benedict Report" (Ex. 35, R. Vol. IV), the testimony of its principal author (at the former trial, in February, 1936), Dr. Murray R. Benedict (R. 432-472), and testimony of Mr. Gustave Momberg (R. 472-494), which was offered at the present trial, as "bringing down to date" the evidence already mentioned.

The Benedict Report deals with the income from farming operations in the District during the years 1929, 1930 and 1931, and contains a supplemental study of the income from a small group of farms in the preceding three years, i. e., 1926-28. Dr. Benedict's testimony was read into the record at the trial of the present proceeding (in November, 1938), failure to produce the witness being waived, but over the objection that the evidence was too remote (R. 432). We cannot here examine this evidence exhaustively, and must content ourselves with a few remarks concerning it:

1. At the time covered by the Benedict Report (which ended seven years prior to the trial of this proceeding), the District, as the Report itself admits (p. 70), was still in the stage of development, and had not been adjusted to the changed conditions arising out of the construction of the irrigation system. The period covered was a panic period, admittedly not typical (R. 451).

2. Since the period covered by the Report, many substantial changes have occurred. Dr. Benedict, testifying at the former trial in April, 1936, agreed that costs of production had declined (R. 471). The agricultural price index which stood at 87 in 1931 (the last year covered by the Report), was at 121 in 1937 (R. 734).

3. The body of the Report is a compilation of the data supplied by the individual and corporate operators of 150 farms in the District, which contains altogether some 2800 farms (R. 470). The 150 farms were drawn by lot from a list of the farms in the District of 20 acres or over, the smaller farms not being sampled at all (R. 470). It is admitted that the data supplied by the farmers was probably biased (R. Vol. IV, p. 24). Not all farms of 20 acres and over were included in the list from which the 150 farms were drawn, some being excluded for reasons that do not very clearly appear (R. Vol. IV, p. 103).

The exclusion from the list of farms sampled of all farms less than 20 acres in size (and others) had the effect that lands in the District representing 61% of the entire assessed value of all lands in the District were eliminated and not sampled at all, the sample being drawn from a group of farms representing 39% of the total assessed value (p. 103).

Figures given for the year 1931, but not given for the two previous years, show (p. 103) that in that year the total delinquency in payment of assessments for the entire District was 17.63%; that the delinquency for the lands from which the sample was taken was

43%, and the delinquency for the lands not sampled, totaling 61% of the entire assessed value in the District was only 1.4%.

The astonishing fact is, therefore, that the entire study represents an examination of a small sample drawn from a group of farms which in the aggregate defaulted 43.73% in the payment of assessments, while the study wholly ignores lands with a total assessed value of 61% of the entire District, which in the same year defaulted only 1.4%. These figures must be derived by calculation from the data given on page 103 of the Report, but the result of the computation given above is indisputable.

4. The data obtained from the farmers varied widely from general experience in the state. For example, the data concerning deciduous fruits (pp. 232-37) indicates low net returns for 1929; but in that year a study made of operations in the same general neighborhood (in Stanislaus County), based on actual and carefully kept records, showed a per acre net profit of $467.50 (R. Vol. IV, p. 102).

5. The Report proceeded on the quite sound theory that due allowance should be made for family labor on farms so operated. But in arriving at the amount properly to be allowed for family labor, the Report achieved results inconsistent with the actual facts, as is now shown. It is rather difficult to follow any particular farm through the various tables in the Report because, although the farms are numbered (as "schedule" No. 244), they are arranged in each table

in a different order, and must be hunted out in order to be traced through the data given.

Space forbids detailed treatment of the matter, but we call attention, as an example, to the farm number 244 in Table 29 (p. 51), which showed a net loss for that farm of $42.40 per acre for the year 1931. Table 27 (p. 49), showing labor charges, stated a total labor charge of $105.00 per acre for this farm of which $7.50 was hired and $92.50 was family labor. Now there are a number of farms shown in Table 27 raising the same crops as farm number 244 but where all of the labor was hired, and the largest sum paid on any such farm where all of the labor was hired was $39.51 per acre (farm number 320, Table 27, p. 51). If the labor charge on farm number 244 is reduced correspondingly, the showing of a loss of $42.40 per acre becomes a profit of $23 per acre. Similar discrepancies could be shown almost indefinitely. From the foregoing we submit that the data contained in this Report (which deals with the period ending seven years before the present proceeding) is at best very slight evidence of present ability to pay.

(g) The testimony of the witness Momberg.

Mr. Momberg's testimony was submitted by the District as "bringing down to date" the Benedict Report.

Mr. Momberg is an employee of California Lands, Inc., a Bank of America subsidiary, and testified only concerning lands which were taken over by fore-

closure by the Bank of America and affiliates. It is admitted that this type of operation is very inefficient (R. Vol. IV, p. 64). Notwithstanding this fact, Mr. Momberg's testimony revealed the fact that the lands operated by him made a net profit over all costs of operation and after payment of assessments during every year of the period concerning which he testified, 1935-38 (R. 481-484, 488).

He testified, moreover, that the District's assessments constituted only five or six per cent of the total operating costs of the farms (R. 494). It is, we submit, apparent even from the foregoing very limited analysis that the District's evidence of ability to pay is of no substantial weight in the present proceeding, and certainly does not in any way impair the force of the evidence furnished by the District's actual experience, which is dealt with in some detail above. It shows that during the entire life of the District the landowners have actually paid assessments sufficient (together with the District's other income) to discharge a debt far greater than the amount offered by the plan.

(h) The market value of the lands charged with payment of the bonds.

It is well known that the market value of property is determined in large measure by its income producing capacity. For this reason it is important to determine the market value of the privately owned lands in the District, chargeable with its debts,

both because that value is directly relevant to the fairness of the plan and because that value is evidence of the extent of the District's ability to pay so far as dependent upon the collection of assessments.

The evidence consists of several items:

(1) As to rural lands, the District itself stated in 1934 that:

> "The average assessed valuation per acre of land for ad valorem tax purposes in the County of Merced is $30.00 per acre. This assessment is about 30 per cent of its market value." (Ex. OO, p. 103.)

This gives a total market value for rural lands in 1934 of over $17,000,000.

(2) The latest figures shown concerning county assessments show an assessed value for rural lands in the District of $12,941,420, and for land in cities and towns in the District of $8,887,583 (R. 719). The California State Board of Equalization, dealing with figures over a period of years (1929-36), states that the ratio of assessed value (for ad valorem tax purposes) to actual value in Merced County varies between 26% and 35% (R. 959-961). Taking the highest ratio, 35%, the actual value in 1936 in the Merced Irrigation District was, for rural lands, just under $37,000,000, and for urban lands $25,393,000, giving a total in excess of $62,000,000 for all lands in the District, urban and rural. Between 1934 and 1937 general conditions improved, and agricultural prices rose over 75 per cent (R. 734).

(3) Turning now to the assessment rolls of the District itself, the latest assessment roll of the District, shown in the record, values the privately owned lands (as of 1937-38) at $11,468,155, which does not include lands deeded to the District for failure to pay assessments (R. 667).

In 1930-31, the District's assessment roll valued the same lands at over $20,000,000 (R. 667). This was reduced by more than $1,000,000 in 1931-32, and was further reduced by more than $6,000,000 in 1932-33. The reasons for this action do not appear other than the fact that negotiations for scaling down the District's debts had begun in 1932, as shown above.

It is significant that improvements (including permanent crops, such as fruit trees, alfalfa, vines, etc., R. 425), are wholly ignored in the assessments made by the District. These improvements, however, are, of course, a part of the security for the bonds. They are ignored in the District's assessments in order to apportion a fair share of taxes to lands allowed to lie idle.

(4) Mr. Momberg (whose testimony was produced by the District allegedly to bring the "Benedict Report", which dealt with the period ending in 1931, down to date) testified that he was the manager of 58 ranches in the District containing a total of 3688 acres, owned by a Bank of America corporation, California Lands, Inc.; that these ranches are scattered all over the District, and raise substantially all the crops grown therein; that the quality of these lands represents a fair average of all the lands in the Dis-

trict; that the lands managed by him are held for sale at an average price of $135 per acre; that this sales price was determined by determining what amount the lands can pay from earnings so as to pay interest on the sale price, and also pay all of their taxes, including District assessments (R. 473, 474, 489, 492, 494).

These figures give a total market value, at the time of trial, of the agricultural lands alone, in excess of $23,000,000.

This value of $23,000,000, it is to be observed, is the value of the lands over and above the encumbrance of the District's bonds.

We submit on the basis of the foregoing, speaking of agricultural lands alone, that the market value of the lands shows that in the opinion of buyers and sellers, these lands have an income producing capacity sufficient to amortize their share of the District's debt and still leave a value of $23,000,000.

IV. THE MEANING OF "FAIR AND EQUITABLE" IN THIS STATUTE.

(a) States seeking bankruptcy relief must provide means for effectuating the requirement that the plan be fair.

In Part V of this brief (headed "Available means for effectuating the requirement of fairness"), it is shown, we submit, that existing California laws pro-

vide adequate means for the carrying out of a plan which will comply with the statutory requirement that the plan be fair, equitable and for the best interest of creditors. The point we now make is this:

In *United States v. Bekins,* 304 U. S. 27, 53, 54, this Court described the municipal bankruptcy provisions as providing for cooperation between State and Nation. The statute requires plans to be fair, equitable and for the best interest of creditors.

We submit that the State's part of the cooperative venture includes the duty of providing means for effectuating the requirement of fairness.

The opinions below show, we submit, that the plan was confirmed on the assumption that unless existing California statutes provide means for giving creditors the benefit of the District's property and income, this plan may be confirmed even though the court believes that (a) the District's corporate properties, and the private property charged with the bonds, each exceeds the total debts sought to be scaled down, and (b) even though the Court believes that the District's average income is sufficient to pay far more than is offered by the plan.

It should not be held, we submit, that a State may demand and receive approval of a plan cutting debts in half on the ground that although the debtor could pay much more, the State has not provided means for enabling it to do so.

(b) The courts below ignored the essential factors determining fairness.

As shown in our petition, neither the findings nor either of the opinions arrive at any conclusion whatever as to:

(1) The value of the District's corporate properties, or

(2) The value of the privately owned lands of the District charged with payment of the bonds, or

(3) The past income of the District as evidencing ability to pay, or

(4) The potential ability of the District to pay, whether present or future.

We submit, therefore, that the decision should not stand unless this Court, upon examination of the evidence, should find that the ultimate facts support the conclusion of the law that the plan is fair, equitable and for the best interest of the creditors.

(c) Both courts below rested their conclusion of fairness on improper grounds.

It is shown in the petition that the Courts below (R. 168, 1015) rested their conclusion that the plan was fair on the following grounds:

(1) That some relief was necessary in 1933 (five years before this action was commenced, R. 174, 1058);

(2) That the surrender to the R. F. C. of 80 per cent of the bonds in 1935 greatly relieved the District's situation (R. 175, 1059);

(3) That the District's present ability to pay (not determined) is largely the result of the R. F. C. loan and the surrender of bonds thereunder (R. 176, 178, 1059);

(4) That the proportion of bonds surrendered (largely in 1935) is irrefutable evidence that the plan is fair (R. 176);

(5) That no modification of the plan is feasible because the Court should not disturb the R. F. C.'s contract, and cannot alter it (R. 178);

(6) That but for the plan, the bonds would be worth less than is offered by the plan (R. 176, 1059-60).

V. AVAILABLE MEANS FOR EFFECTUATING THE REQUIREMENT OF FAIRNESS.

The simple rule of common honesty which this statute enacts by requiring that the plan be fair and equitable is that the Court should not approve a plan whereby the debtor, without surrendering any property, proposes to scale down its debts to less than the value of that property.

This rule is entirely feasible as applied to California irrigation districts. We now enumerate the alternative means whereby the rule can be given effect.

(1) Preliminarily we submit that the statute by requiring that the plan be fair and equitable says in substance that bankruptcy relief is tendered to taxing agencies with the proviso that such relief shall not be granted unless the District can and does propose a plan conforming to the requirement contained in the statute that it shall be fair and equitable within the established meaning of those words.

If the statute is properly so construed, the result in the present case is plainly that the present plan should not be approved.

If it is not approved and no acceptable plan is put forward, the result will be one of two things, both of which have occurred in other districts in California. See *Provident Land Corporation v. Zumwalt,* 12 Cal. (2d) 365, 373:

(a) Actually, the decree would not affect the present condition of the District, quite apart from the fact that the District is already actually refinanced by the R. F. C. loan, for the fact is that the District without doubt would continue to operate under Section 11 of the Districts Securities Commission Act (described above), which permits irrigation districts, which have in the past defaulted, to cease levying assessments for the payment of its debts as they mature and to levy assessments only in such amount as the lands in the District can reasonably pay. The Merced Irrigation District has, in fact, been operating under this statute since 1933 (R. 402, 403).

(b) The other possible alternative, if this plan was not confirmed and no acceptable plan was pro-

posed, would be that the District would levy assessments, take over such lands as defaulted after three years, and resell or rent these lands. This process is described in *Provident Land Corporation v. Zumwalt*, supra, which case also recites the fact that just this has occurred in several districts. The case also holds that all rents or other income received from lands taken over by the District are held by it in trust for the purposes of the Act, namely, for operating expenses and payment of its debts.

There is (we submit) no evidence in the record justifying the conclusion that this would occur even if the District commenced levying assessments sufficient to meet its debts, and even assuming that its debts are as much as it claims them to be.

(2) The second, and perhaps most obvious means for compliance of the California Irrigation Districts with the requirement that the plan be fair is that the District propose a plan for refunding its debt over a longer period than it proposes in fact.

We submit that there is no basis upon which it could be said that it is either fair, equitable or honest for this District to scale down its debts to less than half of their present amount, on the theory that it should pay only so much as it can comfortably pay during the next thirty-five years and should, having done so, be free from all obligation.

The first refunding plan proposed by the Bondholders' Committee, and approved by the electors of the District, proposed a fifty year bond issue (R. 736, 747-50).

(3) As suggested in the opinion of the trial Court (R. 175) and as stated by the Supreme Court of California in *Provident Land Corporation v. Zumwalt*, 12 Cal. (2d) 365, 371, the irrigation districts in California have got into difficulty because of the inexorable requirement that they levy assessments each year sufficient to meet current obligations plus all past defaults. As we have seen, this is no longer true. The point we now make is this:

Merced Irrigation District's difficulties arose out of the statutory requirement for pyramiding debts. The District is peculiarly susceptible to this difficulty because of the fact that its income is very variable. Its income varies not only with farm prices but with the water revenues which it receives.

As a consequence, it is, we submit, plain that a plan should be devised whereby the District's creditors could take advantage of the **average** of the District's fluctuating income. This could be done, and indeed was done, under the first refunding plan approved by the electors of the District by the issuance of callable sinking fund bonds maturing in fifty years (Ex. OO, p. 93). Such a plan would permit the District to make such payments in each particular year as its income justified, and would give its creditors the benefit of the average of its fluctuating income.

(4) Another alternative would be simply to continue doing what the District is doing now, namely, for the District to continue operating under the statute mentioned above, authorizing it, with the approval of the Districts Securities Commission, to levy such

assessments each year as its income for the coming year justified.

(5) The last major alternative is this: Under the California law an irrigation district may voluntarily dissolve, and turn its assets over to a private water company organized for the purpose.

The California Statutes of 1903, page 3, as amended, provide briefly as follows:

Section 1 provides that:

> "Any irrigation district * * * may be dissolved in the manner hereinafter provided * * *"

Section 2 provides for a petition calling for such dissolution and reads in part as follows:

> "Said petition shall also state the assets of said district, including irrigation system, if any, dams, reservoirs, canals, franchises, water rights, a detailed statement of all the lands sold to the district for assessments, and the amount of the assessments on each parcel of land sold, also all assessments unpaid, and the amount upon each lot or tract of land, and all other assets of the district; and in case any proposition has been made by the holders of said indebtedness to settle the same, said proposition, together with any plan proposed to carry the same into execution, shall be included in said petition."

The proposal must be approved by the Superior Court of the State of California (Sec. 5).

Section 7 provides that a corporation may be organized for the purpose of acquiring the assets of the District. That section reads as follows:

"A corporation may be organized under general laws for the purpose of acquiring the assets of said district, including the irrigation system, if any, dams, reservoirs, canals, franchises and water rights, which corporation shall have all the powers, rights and franchises of corporate bodies organized under general laws, and in addition shall have such further powers as may be necessary to possess and carry on said irrigation system and exercise such franchise and water rights."

Section 8 reads as follows:

"The court in its decree shall have power to make the orders necessary to carry out said proposition for the discharge of the indebtedness and distribution of the property of said district, including the right to apportion any indebtedness found due, and to declare said portions liens upon the various parcels and lots of land within the district, and may decree a sale of its assets in such manner as may effectuate said proposition and as the said court may judge best, either in one lot or in such parcels as may be provided, and may provide for conveyance of said irrigation system, including dams, reservoirs, canals, franchises and water rights, and also of any other assets of the district, including lands sold thereto and the assessments due it."

If such a plan were carried out in the present case, the result would be that the bondholders would receive the operating properties of the District (which were paid for by the District with the proceeds of the bonds) and the District's properties would then be operated by the new corporation, owned by the bond-

holders as a public utility. This, because the California statutes provide that:

> "Whenever any person, firm or private corporation * * * sells, leases, rents or delivers water to any person, firm, private corporation, municipality or any other political subdivision of the state whatsoever * * * such person, firm or private corporation is a public utility, and subject to the provisions of the public utilities act of this state and the jurisdiction, control and regulation of the railroad commission of the state of California;" (General Laws of California, p. 4265).

The corporations net power revenue alone would pay what the plan offers in 31 years (R. 933, 938).

VI. IT IS RES JUDICATA BETWEEN THESE PARTIES THAT JURISDICTION TO IMPAIR THE OBLIGATION OF THESE BONDS CANNOT CONSTITUTIONALLY BE CONFERRED UPON A FEDERAL COURT.

In April, 1935, the District filed a petition under the first Municipal Bankruptcy Act (48 Stat. 798, 11 U. S. C., §§301-303), wherein the District sought confirmation of the identical plan here involved (R. 8; Ex. OO, p. 10). Substantially the same bondholders as are petitioners herein appeared in the proceeding as objecting bondholders (Ex. OO, pp. 42-43). The District Court confirmed the plan (Ex. OO, p. 275). Pending an appeal to the Circuit Court of Appeals, this Court decided that the statute was void, in *Ashton v. Cameron County Water Improvement District No. 1*, 298 U. S. 513.

Thereafter the objecting bondholders moved the Circuit Court of Appeals for a judgment reversing the decree of the trial Court with directions to dismiss. The motion was based on the ground that the proceeding rested on the statute, and that the statute had been held void in the *Ashton* case (Ex. 00, p. 333). The motion was granted (R. 106, 89 Fed. (2d) 1002). The District then petitioned this Court for a writ of certiorari (Ex. OO), which petition was denied October 11, 1937 (302 U. S. 709). Thereafter, on July 6, 1937, pursuant to mandate (R. 962), the District Court entered its decree dismissing the cause (R. 965).

After this Court had sustained the present Municipal Bankruptcy Sections (304 U. S. 27) the District, on June 17, 1938, commenced the present proceeding, seeking confirmation of the identical plan, confirmation of which had been sought in the earlier proceeding (R. 8, 36; Ex. OO, p. 10).

We submit that the previous decision between these parties concerning the District's right to confirmation of this plan, seeking to scale down these bonds, is *res judicata* of the rights of the parties.

Briefly stated, our argument is this:

(1) We submit that the substantive rights and powers created by the two statutes are, so far as here involved, identical. We submit further that it now appears from this Court's decisions, that the first statute was valid from the beginning. If this is true, then the second statute simply declared (but did not create) the rights and powers which had already been created by the first statute, and which were still, and are now, in existence.

If this is correct, then the right now asserted is the very right asserted, and held to be no right, in the previous proceeding between these parties.

(2) We submit that even though it were held that, although substantially identical, the second statute nevertheless "recreated" the rights conferred by the first statute (and thereby created a "new cause of action" in the District) nevertheless (we submit), it is settled that a rule of law, which has been announced and applied to a particular relation concerning particular property, is *res judicata* between the parties even though later found to be erroneous, and even though, in the second case, a new cause of action is asserted. See *Tait v. Western Md. Ry. Co.,* 289 U. S. 620, and cases there cited.

(3) We submit that even though this Court now holds that the first statute is void, and that the second is different from the first and valid, the previous judgment between these parties was an adjudication of the rights of the parties under the Constitution, apart from the statute: an adjudication that the Constiuion confers upon these bonds and these petitioners immunity from having them scaled down by the federal bankruptcy court.

(a) The first and second statutes are substantially indistinguishable.

We shall not analyze the two statutes in detail. Both are short, and both were recently considered. We respectfully submit that a mere reading of them

demonstrates that no substantial change in the first is made by the second.

(b) This court did not hold the two statutes to be distinguishable in the Bekins case.

The only part of the Court's opinion in the *Bekins* case which might be taken to distinguish the first statute from the second, is now set out. After quoting from a committee report on the second statute, the Court said:

> "We are of the opinion that the Committee's points are well taken and that Chapter X is a valid enactment. The statute is carefully drawn so as not to impinge upon the sovereignty of the State. The State retains control of its fiscal affairs. The bankruptcy power is exercised in relation to a matter normally within its province and only in a case where the action of the taxing agency in carrying out a plan of composition approved by the bankruptcy court is authorized by state law."

This language might be taken to suggest three distinctions between the two statutes:

(1) It may imply that whereas the second statute does not impinge upon the sovereignty of the states, the first statute did. The fact is, however, that the second statute expresses no more solicitude for the sovereignty of the states than did the first. The first statute (Sec. 80(k)) provides as follows:

"Nothing contained in this chapter shall be construed to limit or impair the power of any State to control, by legislation or otherwise, any political subdivision thereof in the exercise of its political or governmental powers, including expenditures therefor, and including the power to require the approval by any governmental agency of the State of the filing of any petition hereunder and of any plan of readjustment, and whenever there shall exist or shall hereafter be created under the law of any State any agency of such State authorized to exercise supervision or control over the fiscal affairs of all or any political subdivisions thereof, and whenever such agency has assumed such supervision or control over any political subdivision, then no petition of such political subdivision may be received hereunder unless accompaned by the written approval of such agency, and no plan of readjustment shall be put into temporary effect or finally confirmed without the written approval of such agency of such plans." (11 U. S. C., Sec. 303(k).)

In addition, Section 80(c) reads in part:

"[the court] shall not, by any order or decree in the proceeding or otherwise, interfere with (a) any of the political or governmental powers of the taxing district." (11 U. S. C., Sec. 303(c).)

The provision of Section 80(k), quoted above, was quoted in full in the *Ashton* case (298 U. S. 513, 526).

(2) The above quotation from the Court's opinion in the *Bekins* case might be taken to imply that the statutes are distinguishable on the ground that in the second, "the bankruptcy power is exercised in rela-

tion to a matter normally within its province"; and that this is not true of the first statute. But this could not have been the Court's meaning, for plainly, if the second statute is within the province of bankruptcy, so is the first. This indeed was in effect held to be true in the *Ashton* case, where the Court said that the first statute "is adequately related to the general 'subject of bankruptcy'" (298 U. S. 513, 527).

(3) The passage quoted from the Court's opinion in the *Bekins* case might be taken to imply that there was some distinction between the two statutes concerning the consent of the state to proceedings thereunder. The rest of the opinion in the *Bekins* case, however, makes it perfectly clear that no such distinction was intended to be drawn.

(c) The court's failure expressly to overrule the Ashton case is not here significant.

The only remaining circumstances which might suggest that in the *Bekins* case the Court meant to distinguish the later statute from the earlier, is the fact that the Court did not in so many words overrule the *Ashton* case. The inference would (we submit) be unsound, both because (in view of the above discussion) it would be unreasonable in fact to distinguish them, and for the additional reason now discussed.

The considerations which guide the Court in administering the doctrine of *stare decisis* are wholly different from, and have no bearing on, the rules

which govern application of the principle of *res judicata.* In the language of Mr. Justice Brandeis, "stare decisis is not, like the rule of res judicata, a universal and inexorable command" (285 U. S. 393, 405).

The Courts are, of course, free to overrule earlier decisions of which they disapprove. But the fact that an earlier decision is later departed from does not impair its effect as *res judicata* in any respect.

Frequently, when the Court has not finally determined that an earlier decision should be finally disapproved, it is thought preferable to explain or distinguish it, and to leave its final disposition as a precedent to a later time. For example, the Court often announces that an earlier decision *has been* overruled, referring to intermediate decisions which did not do so in terms, but simply distinguished or explained away the earlier decision so far as necessary. See, for example:

Morgan v. United States, 113 U. S. 476, 496;
Leisy v. Hardin, 135 U. S. 100, 118;
Brenham v. German Amer. Bank, 144 U. S. 173, 187;
Terral v. Burke, 257 U. S. 529, 533;
Lee v. Chesapeake & O. Ry., 260 U. S. 653, 659.

Decisions by a divided Court are considered to be of only limited authority, so far as concerns the rule of *stare decisis* (*Legal Tender Cases,* 12 Wall. 457, 553-554), although the fact that the Court was divided would not, of course, affect the force of the earlier decision as *res judicata,* in any manner or degree.

There is a considerable body of opinion that in the field of constitutional law, the doctrine of *stare decisis* is of much less force than it is in general. See the statement by Mr. Chief Justice Taney in *The Passenger Cases,* 7 How. 283, 470; and also the discussion and authorities in the dissenting opinions of Mr. Justice Brandeis in

> *State v. Dawson,* 264 U. S. 219, 238;
>
> *Burnet v. Coronado Oil & Gas Co.,* 285 U. S. 393, 405, et seq.

See, also,

> *Erie R. Co. v. Tompkins,* 304 U. S. 64, 77;
>
> Warren, *Supreme Court in the U. S. History* (ed. 1928) II, 748-749;
>
> *Goodhart,* "Case Law in England and America", 15 Corn. L. Q., 173, 179-180;
>
> 1 *Willoughby, Constitutional Law* (2 ed.) Sec. 44.

The rule of *res judicata,* on the other hand, is a very different matter. It has nothing to do with the policy of judicial administration embodied in the doctrine of *stare decisis.* It is a plain and unqualified rule of law. In the language of this Court,

> "It is a fundamental principle of jurisprudence, arising from the very nature of courts of justice and the objects for which they are established, that a question of fact or of law distinctly put in issue and directly determined by a court of competent jurisdiction cannot afterwards be disputed between the same parties. *Southern Pacific Railroad v. United States,* 168 U. S. 1, 48." (Frank v. Mangum, 237 U. S. 309, 333.)

The considerations which lead courts to follow, or overrule, or distinguish, or ignore, or brush aside a precedent, simply have no relevancy when a prior decision is invoked as *res judicata* between the parties.

The question, therefore, whether the prior decree between these parties is *res judicata,* is in no way affcted by the answer to the question whether or not the *Ashton* case is still a living precedent.

(d) The substantive rights described in the second statute already existed under the first, and were adjudicated upon in the first action between these parties.

When this Court declares that a statute is invalid, its judgment does not destroy the statute, does not undo the enactment by the Congress and its approval by the Executive; the Court simply decides the controversy before it according to applicable rules of law, and applies the paramount law governing the case, namely, the Constitution.

Marbury v. Madison, 1 Cranch, 137, 176.

If, therefore, the Court later alters its opinion of the matter, it follows that the statute is thenceforth known to have been valid from the beginning. See authorities collected in

"Status of District of Columbia Minimum Wage Laws", 39 Ops. Atty. Gen. 4.

It follows that if the views announced in *United States v. Bekins,* 304 U. S. 27, call for the conclusion that the first municipal bankruptcy enactment is not

inconsistent with the Constitution, then that statute was a valid enactment from the beginning, and still is a part of the law unless it has been repealed by the Congress.

The first statute certainly was not repealed by the second, for the latter declares in terms that it

> "shall not be construed as to modify or repeal any prior, existing statute relating to the refinancing or readjustment of indebtedness of municipalities, political subdivisions or districts." (Sec. 83(h), 11 USC, Sec. 403(h).)

Even if the first statute had been repealed by the second, it is plain that the second would be taken simply to continue the substantive rights created by the first: The same section just quoted makes this clear, by providing (what would otherwise be unnecessary), that the initiation of proceedings under the former statute "shall not constitute a bar to the same taxing agency or instrumentality initiating a new proceeding", under the new statute. We submit that the provision just quoted omits, *ex industria,* to say that *final judgment* under the first statute shall not bar proceedings under the second.

The only other act of Congress which might be taken to repeal the first statute is the act of June 22, 1938 (52 Stat. 840, 939-40), wherein Congress either deprives the first act of its chapter number in the bankruptcy act (by numbering the new statute as Chapter IX), or adds the new provisions to the chapter containing the old.

Assuming this to intimate that Congress believed the decision of this Court in the *Ashton* case had de-

stroyed the first statute, that intimation, if erroneous, does not operate as an enactment of Congress' opinion.

Endlich, Interpretation of Statutes, Sec. 372;
United States v. Claflin, 97 U. S. 546, 548;
District of Columbia v. Hutton, 143 U. S. 18, 27.

We submit, therefore, that the statute which is the basis of this proceeding did not create new substantive rights; that the substantive rights which the District here asserts were created by the first statute, and were the subject-matter of the adjudication in the former action between these parties, which rights are therefore *res judicata.*

(e) Even though the new statute re-created the rights created by the first, the matter is res judicata.

It is apparent from the foregoing that if the first statute was valid from the beginning, then even though the second statute is said to have re-created the substantive rights created by the first, even so, the adjudication concerning the nature and scope of those rights in the prior proceeding between these parties is *res judicata* in the present proceeding.

A common application of principles applicable here is contained in decisions concerning the validity or scope of tax statutes. The levy of taxes is, of course, a purely legislative act.

Cooley on Taxation, Secs. 1012-1013;
Heine v. Board, 19 Wall. 655;
Merriweather v. Garrett, 102 U. S. 472;
Taylor v. Secor, 92 U. S. 575.

Obviously, a levy of taxes for one year is a distinct legislative act from levies concerning later years; and the liability for taxes under one levy is a different cause of action from the liability for taxes for other years. It is nevertheless settled that an adjudication of the existence or scope of the taxing power (as to a particular litigant) is *res judicata* of taxes for later years, under later tax levies and later tax statutes.

Tait v. Western Md. Ry. Co., 289 U. S. 620.

As was said in *New Orleans v. Citizens Bank,* 167 U. S. 371, 400:

> "It is undoubtedly true that the taxes of each year ordinarily constitute separate and distinct rights or causes of action. But where an action is brought to recover taxes paid in one year, and an action is afterwards brought to recover for the taxes paid in a subsequent year, and the adjudication in the first is pleaded as a bar to the recovery in the second action, the question whether the estoppel is effectual will depend upon the issues in the two actions.
>
> "If the right to recover and the defense thereto are based upon precisely the same ground, why litigate again the question that has been determined? In such case the very right of the matter has been determined by a court of competent jurisdiction. It is not essential that the causes of action should be the same, but it is essential the right or title should be; that is, the issues in both actions and the matter on which the estoppel depends must be the same, or substantially so."

(f) Even though the second statute be taken to create new and different rights, the previous judgment is res judicata, because it determines the nature of the obligation of these bonds under the Constitution.

There is, we submit, no room for doubt concerning the scope of this Court's decision in the *Ashton* case. As shown above, the previous decision between these parties rested solely upon the authority of the *Ashton* case. This Court's decision in that case was not rested upon any particular provision of the first Municipal Bankruptcy Statute, but directly upon the Constitution. The Court announced the simple proposition that bonds like those here involved are immune under the Constitution from being scaled down by a federal Court in bankruptcy. The Court said in part:

> "We need not consider this Act in detail or undertake definitely to classify it. The evident intent was to authorize a federal court to require objecting creditors to accept an offer by a public corporation to compromise, scale down, or repudiate its indebtedness without the surrender of any property whatsoever. * * *
>
> "Our special concern is with the existence of the power claimed—not merely the immediate outcome of what has already ben attempted. * * *
>
> "The especial purpose of all bankruptcy legislation is to interfere with the relations between the parties concerned—to change, modify or impair the obligation of their contracts. The statute before us expresses this design in plain terms. It

undertakes to extend the supposed power of the Federal Government incident to bankruptcy over any embarrassed district which may apply to the court. * * *

"Neither consent nor submission by the States can enlarge the powers of Congress; none can exist except those which are granted. *United States v. Butler,* decided January 6, 1936, 297 U. S. 1. The sovereignty of the State essential to its proper functioning under the Federal Constitution cannot be surrendered; it cannot be taken away by any form of legislation. See *United States v. Constantine,* 296 U. S. 287. * * *

"* * * for a very long time this court has steadfastly adhered to the doctrine that the taxing power of Congress does not extend to the States or their political subdivisions. The same basic reasoning which leads to that conclusion, we think, requires like limitation upon the power which springs from the bankruptcy clause. *United States v. Butler, supra.*"

We respectfully submit that until it is announced that decisions of this Court, wherein it changes its views on constitutional questions, amount to amendments of that document, it will not be proper to hold that litigants must re-litigate rights determined on constitutional grounds later abandoned by the Court.

VII. RECONSTRUCTION FINANCE CORPORATION'S CONSENT TO THE PLAN SHOULD NOT BE COUNTED AGAINST THESE PETITIONERS, BECAUSE IT IS IN A DIFFERENT CLASS OF CREDITORS.

It is perfectly apparent that the R. F. C.'s interest in the District is both different from and adverse to the interests of these petitioners. Moreover, under the plain language of the statute (we submit), the R. F. C. is in a different class of creditors from the objecting bondholders.

(a) The R. F. C. is a secured creditor.

The Bankruptcy Act, Section 83(b), provides:

> "The holders of claims for the payment of which specific property or revenues are pledged, or which are otherwise given preference as provided by law, shall accordingly constitute a separate class or classes of creditors."

The R. F. C. contract provides that the R. F. C. shall not be obligated to make the loan

> "unless the Borrower shall provide for the allocation of funds and income derived from the sale of electrical power by the Borrower to the payment of the loan authorized by this Resolution in an amount and manner satisfactory to the Division Chief and Counsel." (Ex. OO, pp. 177-8.)

And the final refunding bond purchase contract (Ex. OO, p. 202) provides for the allocation of power revenue to the maintenance of a reserve fund, and to the ultimate payment of the refunding bonds (Ex. OO, pp. 208-210).

This reserve fund was created, and now contains over $1,000,000 (R. 669). Indeed, it was adjudicated in a proceeding brought to validate the proposed refunding bonds to be issued to the R. F. C. (an *in rem* proceeding, R. 597-611),

> "that said district has duly and regularly created said Reserve Fund and duly and regularly allocated certain of said power revenues, as hereinbefore set forth, and is and has been duly authorized to create said Reserve Fund and to make said power revenue allocation, and that the same, and each of them, are valid and binding obligations of said district." (R. 597, 611.)

No amount of refined logic can obscure the fact that the debt owing to the R. F. C., whatever its amount and however it be evidenced, is secured by a very large amount, and has been so secured ever since it became a creditor in any imaginable sense. And under the inescapably plain language of the statute, such a creditor (even assuming it is otherwise in the same class with us), must be classified in a different class from creditors who, like the objecting bondholders, are not similarly secured.

In short the R. F. C. has (in this particular case), voluntarily contracted itself into a different class of creditors from the objecting bondholders.

(b) The R. F. C.'s interest in the District is both different from and adverse to the interests of these petitioners.

This statute, like the other similar acts, requires that the judge "shall classify the creditors according to the nature of their respective claims and interests" (Sec. 83(b)).

It plainly appears from what has been said above that the R. F. C.'s interest in the District is both different from and adverse to the interests of the objecting bondholders:

(1) As shown above, the plan gives the R. F. C. all that it is entitled to in any event, the plan being indeed based directly on, and in effect incorporating, the R. F. C.'s contract with the District (R. 28).

(2) This being true, it would injure the interests of the R. F. C. if the objecting bondholders received more than the amount offered by the plan, since the District's ability to pay the R. F. C. would, to that extent, be impaired.

VIII. THE BONDS HELD BY R. F. C. ARE OBLIGATIONS OF THE DISTRICT ONLY AS SECURITY FOR THE R. F. C. LOAN.

THE DISTRICT'S DEBT IS THEREFORE ONLY HALF WHAT IT CONTENDS.

Years before the passage of the statute upon which this proceeding rests, some 90 per cent of the District's old bondholders effected an accord and satis-

faction with the District, and a relation was established between R. F. C. and the District at that time whereby (we say) the District owes the R. F. C. only the amount advanced by that corporation, holding the surrendered old bonds in pledge as security. The District's whole case rests on its contention that the R. F. C. is a creditor to the full amount of the bonds held by it, either by the terms of its contract with the R. F. C. or by the terms of the statute, or both.

We submit that such a construction of either would be unfair and unreasonable. Even if the contract so provided, it was not then lawful (in 1934) for a debtor and creditor to contract that as against other creditors, a debt should be doubled; and even if the statute (passed years later) enacted that proposition, it does not purport to be retrospective.

(a) As between R. F. C. and the District, the amount owing R. F. C. is only the amount loaned.

We now consider the contract as a contract, i. e., apart from any peculiar effect it may have in a bankruptcy proceeding like this.

The R. F. C. now holds $14,686,000, principal amount, of the District's bonds (R. 32). The total amount advanced by the R. F. C. under its contract with the District is $7,570,871.60 (R. 88).

The negotiations between the District and R. F. C. resulted in the execution of eight documents:

1. The original R. F. C. resolution (Nov. 14, 1934) (Ex. OO, pp. 155-79);

2. Acceptance thereof by petitioner (Dec. 11, 1934) (Ex. OO, pp. 180-2);

3. An amendment of the R. F. C. resolution (July 6, 1935) (Ex OO, pp. 192-3);

4. Acceptance thereof by petitioner (July 23, 1935) (Ex. OO, pp. 194-7);

5. An "Agreement" between R. F. C. and the petitioner (Aug. 14, 1935) (Ex. OO, pp. 217-21);

6. The "Bond Purchase Contract" (Sep. 16, 1935) (Ex. OO, pp. 202-17);

7. A second amendment to the original R. F. C. resolution (about Sept. 17, 1935) (Ex. OO, pp. 193-4);

8. Acceptance thereof by petitioner (Sept. 18, 1935) (Ex. OO, pp. 198-201).

Final completion of the contract eliminated one of these documents, namely that numbered 5 above: The "Bond Purchase Contract", which provides for the purchase of refunding bonds, incorporates, by reference, the R. F. C. resolution (No. 1, above) and the District's acceptance thereof (No. 2, above); and provides:

> "This contract, together with the Resolution of R.F.C. herein referred to, and also the resolution of the Borrower, herein referred to, contain the entire agreement between the parties * * *" (Ex. OO, p. 216).

(b) The contract is governed by California law.

The contract between the R. F. C. and the District provides in terms that "This contract * * * shall be governed by and construed in accordance with the laws of the State of California" (Ex. OO, p. 216).

(c) The contract creates a debt equal to the amount loaned.

In every document constituting the loan contract the transaction is spoken of as a "loan" (see, e. g., Ex. OO, pp. 155, 156, 157, 158). The original R. F. C. resolution recites that the Merced Irrigation District "(herein called the 'Borrower'), has applied to this Corporation for a loan" (Ex. OO, p. 155). The parties have repeatedly, in correspondence and otherwise, made it clear that as between the District and the corporation, the transaction is considered to be a loan, by virtue of which the District owes the R. F. C. the amount loaned, and no more (see, e. g., R. 774, 778, 792, 796, 759, 762, 799, 818, 821). The list of such references could be multiplied almost indefinitely.

The contract provides in part (Ex. OO, p. 165):

> "if the Borrower shall, before any New Bonds are delivered to this Corporation, pay or cause to be paid to this Corporation an amount equal to the disbursements it has made to or for the benefit of the borrower with 4% interest thereon until paid, this Corporation will thereupon surrender or cause to be surrendered the Old Securities then held by it or on its behalf to the Borrower."

The R. F. C. has no authority to purchase bonds, but only to make loans. The only authority of R. F. C. to participate in such transactions is Section 36 of the Emergency Farm Mortgage Act (43 U. S. C., Sec. 403); the statute simply authorizes loans, which must be secured.

(d) No contract provision contradicts the provisions creating a secured loan.

The contract provides, among other things, as follows:

> "All disbursements made by this Corporation for the purpose of acquiring the Deposited Securities, or rights in or to the same, shall be deemed to be and shall constitute disbursements from the loan authorized herein" (Ex. OO, p. 158).

Disbursement is to be made—

> "to or for the benefit of the Borrower through the purchase of securities issued or to be issued by the Borrower or upon promissory notes collateraled by the obligations of the Borrower * * *" (Ex. OO, p. 159(b)).
>
> "All or any part of the Old Securities acquired or held * * * through any disbursement * * * as well as all rights in or to such Old Securities may be kept alive for a greater or lesser time and for any purpose the Division Chief and Counsel may deem necessary" (Ex. OO, p. 164(c)).
>
> "* * * Until such Old Securities have been exchanged for New Bonds, all such securities as well as all rights in or to the same shall continue to be and constitute obligations of the Borrower

> for the full amount thereof and nothing in this resolution shall be deemed to limit the right of this Corporation to enforce or cause to be enforced full payment of principal and interest of such Old Securities as and when the Division Chief and Counsel shall deem it advisable to do so * * *" (Ex. OO, pp. 164-165).

The District contends that these provisions actually make the R. F. C. a creditor of the District to the full amount of the bonds including unpaid interest. This argument necessarily says in effect that the contract meant one of two things (although it does not say which):

1. "In consideration of the loan of so much, the borrower agrees to pay either the amount borrowed or approximately twice that amount, as the lender may elect", or

2. "As between ourselves, the RFC must accept refunding bonds in the amount loaned; but as against any holder of old bonds who refuses to surrender them, the parties hereto may assert that the full amount of the old bonds surrendered are an actual debt of the borrower to the RFC."

Neither of these constructions is tenable, for a number of reasons:

(a) Both would be illegal, and void for the excess over the actual debt, under the California law, which governs by express provision (Ex. OO, p. 216).

(b) Both would be grossly usurious, and void for the excess as a penalty (*Cal. Const.*, Art XX, Sec. 22;

3 *Williston on Contracts* (2d Ed.), Sec. 781; 5 id., Sec. 1407).

(c) The second construction would be contrary to the plain language of the contract. This, because there is not even a suggestion that the R. F. C.'s alleged option to demand double payment shall cease if all of the old bonds are brought in. On the contrary, the R. F. C.'s apparent discretion is absolute. Indeed, the clause says so; it says that if in any way the R. F. C. should "acquire legal title to all, or any part" of the old bonds, then "in its discretion" the R. F. C. may keep the old bonds alive "for any purpose" (Exhibit OO, p. 203).

In other words, if the provision in question is taken to give the R. F. C. the right, at its election, to demand full payment of the old bonds, then inescapably the R. F. C. has that power in any event, i. e., whether all of the old bonds are surrendered or not. It follows that the second of the two possible constructions for which appellee contends is contradicted by the contract itself.

(d) But the first possible construction (set out above) is, in addition to being illegal under California law, simply fantastic, and contrary to common sense.

It is significant, therefore, that an alternate and entirely reasonable interpretation of the provision is possible, namely, this:

The parties intended, we submit, to provide by this provision that the R. F. C.'s **security rights** in the old

bonds shall include the full rights of an owner, up to, and as security for, the amount owing. Although the R. F. C. would probably have those rights as pledgee without express provision, an express provision is nevertheless both natural and desirable, as is shown by the large amount of litigation that arises, in cases of partial refinancing, over this precise question, namely, the question whether one who has made a loan to a debtor on the security of part of an old bond issue may assert, **as security for the loan** the rights of an outright owner of old bonds. See the many cases on the question discussed in 47 *Harvard Law Review,* 1093-1126, and 81 A. L. R. 139-146.

(e) No provision in the statute (we submit) permits debts extinguished before its enactment to be revived for the purposes of this proceeding.

Section 82 of the Bankruptcy Act (11 U. S. C., 402) provides in part:

> "Any agency of the United States holding securities acquired pursuant to contract with any petitioner under this chapter shall be deemed a creditor in the amount of the full face value thereof."

The earlier Act contained no such provision. And Section 83(j) of the Act reads as follows:

> "The partial completion or execution of any plan of composition as outlined in any petition

> filed under the terms of this Act by the exchange of new evidences of indebtedness under the plan for evidences of indebtedness covered by the plan, whether such partial completion or execution of such plan of composition occurred before or after the filing of said petition, shall not be construed as limiting or prohibiting the effect of this Act, and the written consent of the holders of any securities outstanding as the result of any such partial completion on execution of any plan of composition shall be included as consenting creditors to such plan of composition in determining the percentage of securities affected by such plan of composition."

Section 83(j), just quoted, was added to the statute by an amendment of June 22, 1938, and went into effect three months later, i. e., on September 22, 1938 (52 Stat. 840, 940).

The R. F. C.'s consent to the plan here proposed was executed June 8, 1938 (R. 6, 32). This action was commenced June 17, 1938 (R. 8, 36). We submit that this statutory provision, enacted after the action was commenced, cannot add to or change the effect of the R. F. C.'s consent to the plan.

The provision quoted above from Section 82 should not (we submit) be construed as providing that even though the District's debts have been reduced by half (through an accord and satisfaction with most of its old bondholders) followed by a pledge of the old bonds as security for a loan, all before the statute was passed, nevertheless, for purposes of bankruptcy proceedings, the District is to be treated as if it still

owed the amount which it owed, in fact, some years before the proceeding was commenced.

As we presently show, the R. F. C. has ample powers to participate in refinancing transactions without the aid of a statute so construed. Moreover, an alternative, and an entirely reasonable construction, is available.

(1) The Court may doubtless take judicial cognizance of the fact that R. F. C. does advance money in aid of refinancing schemes without reducing the obligations of the debtor until after the scheme has been carried out. Thus, it may postpone actual disbursement; or it may make a loan to a trustee or committee for the bondholders (secured by the old bonds), waiving personal liability. This latter method was employed in at least one case, *Leuhrmann v. Drainage Dist. No. 7,* 21 Fed. Supp. 801, 802.

The R. F. C. is, in short, in no need of so drastic a provision as this one would be if construed as the District contends it should be.

(2) Another and entirely reasonable construction is available: The statute (Section 82) defines the term "creditor" as a "holder" of securities.

Now a pledgee is, of course, a "holder" of the securities held in pledge. But the pledgee's status as a holder does not increase the debts of the pledgor, even though the securities held in pledge are the pledgor's own obligations.

The law on this question appears to be fairly clear. Although the transaction is anomalous, it appears to

be settled that a debtor may pledge its own bonds: As security for his promise to pay $1000, a debtor may pledge an instrument which is simply another promise by him, to pay another $1000. When it does so, the pledgee may realize on (i. e., obtain a judgment upon) the pledged promise, in addition to obtaining a judgment on the main promise, as security for which the instrument was pledged. But the pledgee may, of course, obtain only one satisfaction, that is to say, may actually collect only the amount actually owing.

> *Anglo-California Trust Co. v. Oakland Railways,* 193 Cal. 451;
> *Murphy v. Murphy,* 74 Conn. 198.

In the event of bankruptcy proceedings, moreover, the only amount which the pledgee may prove is the amount owing on the actual debt.

> *Sauve v. Fleschutz,* 219 Fed. 542;
> *Butterfield v. Woodman,* 223 Fed. 956;
> *In re Sullivan Condensed Milk Co.,* 291 Fed. 66.

Taking account of this rule, we submit that the provision of the Municipal Bankruptcy Act under inquiry (providing that a public agency holding securities pursuant to contract with the petitioner shall be deemed a "creditor", i. e., a holder, in the amount of "the full face value thereof"), should be taken simply to codify the rule just discussed.

In other words, the provisions should be taken to mean that a public agency which makes a loan in aid of a refinancing scheme, taking the old bonds sur-

rendered as security for its loan, shall have the remedies of any holder of bonds for the purpose of insuring repayment of its loan.

(3) The statute might also be reasonably construed as settling the much vexed question of the rights of a pledgee of a corporation's own bonds as against outright owners of similar bonds. It is obviously possible to hold either (a) that such a pledgee can claim a proportion of assets measured by the amount of his actual debt, or (b) that as against other creditors he is entitled to a proportion of assets equal to the proportion which the securities held by him in pledge bear to all similar securities. See the many cases on this question discussed in 47 *Harvard Law Review*, 1122; 81 A. L. R. 146.

This statute settles the choice between these alternatives.

(f) The bondholders who surrendered their bonds did so irrevocably.

There is no doubt of the proposition stated in the heading. The District has never argued, and we assume will not now argue, that the old bondholders can ever again assert any interest in the bonds surrendered by them (in 1935, for the most part). They were each required to execute "A Memorandum of Sale and Receipt" upon being paid 51.501¢ on the dollar of principal, wherein they unconditionally sold the old bonds and accepted the amount paid "in full payment therefor" (R. 571, 572).

IX. IF THE PLAN IS CONFIRMED, IT SHOULD IN ANY EVENT BE ON CONDITION OF PAYMENT TO OBJECTING BONDHOLDERS OF FOUR PER CENT INTEREST.

This plan tells the bondholder that he must accept the amount offered in full satisfaction of an undisputed debt, or else forego the enjoyment thereof for such number of years as it will take to litigate it, receiving no interest in the meantime. Such a plan is contrary, we submit, to the purposes of the statute, which certainly was not intended to permit petitioning districts thus to subject their bondholders to substantial coercion in order to induce acceptance of plans believed by the bondholders to be unfair. See:

> *Manning v. Brandon Corporation*, 163 So. Car. 178.

The money necessary to carry out the plan first became available for tender to the bondholders on October 4, 1935 (R. 344), and the major portion of the bondholders then surrendered their bonds and received the cash (R. 344). Since then the District has paid the R. F. C. 4% interest on the amount advanced.

The plan (R. 28) does not contemplate payment of any interest to objecting bondholders. If it is confirmed, and confirmed unconditionally, they will receive only the amount of the cash offer, without interest.

We submit that denial of any interest to objecting bondholders makes the plan unfair; and if confirmation of the plan is to stand, the decree should make the confirmation conditional upon payment to objecting bondholders of 4% interest from the time of the first

disbursement to consenting bondholders. This for the following reasons:

(1) In the first place, there is no question but what a bankruptcy court, as a court of equity, has power to impose conditions, on equitable principles, so long as those principles are not inconsistent with the Bankruptcy Act.

> *Securities & Exchange Commission v. U. S. Realty & Improvement Company,* ...... U. S. ......, 60 S. Ct. Rep. 1044, 1053-4.

The principle that an equitable decree must not be unfair is not only a fundamental principle of equity but an express command of this statute. This being true, this Court's power to grant the relief on conditions which will make its operation fair and equitable is not only within its power but a part of its duty.

(2) Secondly, and apart from the foregoing, we submit that the Act should not be construed as authorizing a plan (as here) whereby the bondholders' unquestioned right to object to the plan, and to ask for judicial examination of its fairness, is seriously handicapped and penalized by the plan itself.

(3) It is important to observe that payment of interest to the objecting bondholders will not require the District to make any payment whatever beyond what the plan itself contemplated. The central theory of the plan is that the District proposes to borrow money at 4% wherewith to discharge its bonds at 51.501¢ on the dollar. The actual operation of the plan under the decree is that the District saves 4% for five years on the entire amount admittedly owing to the

objecting bondholders (by the very terms of the plan) from the beginning; and they in turn are penalized in an equal amount by being deprived of both the use of their money and interest thereon during the entire period of litigation.

Surely the District should not thus profit, nor should the objecting bondholders thus suffer (as compared with consenting bondholders), solely because they objected to the plan on the ground that they believed it to be unfair.

(4) The most obvious analogy to the present situation in private law is the effect of a tender as stopping interest. It is settled that a conditional tender does not stop the running of interest.

6 *Williston on Contracts* (Rev. Ed.) 5144.

More particularly, a tender on condition that the creditor surrender a right then in litigation between the parties is no tender at all, and is ineffective, therefore, to stop the running of interest.

Cameron County Improvement Dist. No. 8 v. De la Vergne, 100 F. (2d) 523.

So here, the plan was in substance a tender to the bondholders of much less than half the amount owing to them (taking account of unpaid interest), made on condition that the amount tendered be accepted in full satisfaction of the debt. Whether or not the bondholders were bound to accept the amount tendered as full satisfaction (i. e., whether or not the plan was "fair") was, as a matter of law, a question which the bondholders could with entire justice and propriety dispute.

For the foregoing reasons, we submit, to say that the offer of the plan stopped the running of the interest on the amount ultimately found owing is contrary to the reasonable construction of the statute, is eminently unfair and inequitable, and is contrary to analogous rules of law.

We earnestly submit, therefore, that if the plan is to be confirmed, this Court should impose, as a condition to affirmance, that the objecting bondholders be paid interest at 4% from the date of the original disbursement by the R. F. C. (October 4, 1935, R. 344) to the date of actual payment.

X. THE STATE PROCEEDING UNDER A STATE INSOLVENCY LAW, STILL PENDING BETWEEN THESE PARTIES, MAY BAR THIS PROCEEDING.

On May 25, 1936, this Court held that the first Municipal Bankruptcy Act was void, in the *Ashton* case (298 U. S. 513). On March 30, 1937, a California statute was approved, effective immediately, entitled "Irrigation District Refinancing Act" (Cal. Stats. 1937, pp. 92-101). It provides for submission to the state courts by irrigation districts of refinancing plans. If the plan is found to be fair, an interlocutory judgment is entered. This judgment purports to establish the public necessity for condemnation of non-consenting bonds, and the case then proceeds as an ordinary condemnation proceeding, at which the value of the bonds is determined, but must not be found to exceed the amount offered by the plan. Upon pay-

ment of the value so fixed, the bonds are taken for public use.

Thereafter, on August 16, 1937, Congress enacted the present Municipal Bankruptcy provisions (50 Stat. 654), which were held to be valid by this Court in *United States v. Bekins,* 304 U. S. 27, on April 25, 1938. On June 17, 1938, the present proceeding was commenced (R. 8, 36).

Notwithstanding the pendency of the present proceeding, the District, on March 10, 1938, commenced a proceeding under the state statute described above, presenting to the Court the identical plan here involved (R. 381-3). After this Court sustained the second municipal bankruptcy statute, the District suspended action in the state proceeding, which is still pending. In the present proceeding, we pleaded the pendency of this state court proceeding (R. 48, 66, 67, 69, 70, 123).

We submit that the California statute in question is void under the rule laid down in *Sturges v. Crowninshield,* 4 Wheat. 122.

If it is valid, however, the question is presented whether the plea of another action pending was good. There is not, so far as we know, any controlling authority on the question whether or not, in such a situation, a state proceeding under a valid state insolvency law, pending at the time the Congress occupies the field under its bankruptcy power by enactment of or amendment to a bankruptcy law, is superseded by the federal statute.

If we are right in our contention (point VI, supra) that the first Municipal Bankruptcy Act, passed prior to the enactment of the state statute, is now known to have been valid from the beginning, then we submit that the state statute is void, not only as an impairment of the obligation of contract, but also because the field which it endeavors to invade was already occupied by the federal statute.

XI. IT IS NOW SETTLED BY LOCAL LAW THAT THE FUNCTIONS OF CALIFORNIA IRRIGATION DISTRICTS ARE STRICTLY GOVERNMENTAL.

Since the decision of this Court in *United States v. Bekins,* 304 U. S. 27, the Supreme Court of California has said of irrigation districts that their "functions are considered exclusively governmental; their property is state owned, held only for governmental purposes * * *" (*El Camino Irrigation District v. El Camino Land Corp.,* 12 Cal. (2d) 378, 383). See also:

Moody v. Provident Irrigation District, 12 Cal. (2d) 389, 395;

Anderson-Cottonwood Irrigation District v. Klukkert, 13 Cal. (2d) 191, 197.

It is also true that in *Peoples State Bank v. Imperial Irrigation District,* ...... Cal. (2d) ......, 99 Cal. Dec. 317, the State Supreme Court upheld the California statute consenting to proceedings like this one.

That decision, however, rests on the proposition (mistakenly, we submit) that this Court's decision in

the *Bekins* case settled the validity, under both state and federal Constitutions, of such state statutes.

We submit that all these cases taken together raise the question whether or not it can now be said that the Municipal Bankruptcy Act confers jurisdiction of proceedings like this one, affecting California irrigation districts: This in view of the provisions of the federal statute (Sec. 83(i)), that

> "Nothing contained in this chapter shall be construed to limit or impair the power of any State to control, by legislation or otherwise, any municipality or any political subdivision of or in such State in the exercise of its political or governmental powers, including expenditures therefor.";

and the provision of Section 83(c) that the judge

> "shall not, by any order or decree, in the proceeding or otherwise, interfere with (a) any of the political or governmental powers of the petitioner; or (b) any of the property or revenues of the petitioner necessary for essential governmental purposes; or (c) any income-producing property, unless the plan of composition so provides.";

and in view of the proposition that the Congress has no authority to alter the division of powers between State and Nation, even though a particular state (or all the states) consent.

CONCLUSION.

It is submitted that the writ of certiorari should be granted, the decree of the Court below reversed, and the proceeding directed to be dismissed.

Dated, San Francisco, California,
November 18, 1940.

Respectfully submitted,
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Due service and receipt of a copy of the within is hereby admitted

this...day of November, 1940.

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Counsel for Respondent.

End